

ORIGINAL

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

The New PJM Companies:	)	Docket Nos.	ER03-262-001
American Electric Power Service Corp.	)		ER03-262-004
On behalf of its operating companies	)		ER03-262-005
Appalachian Power Company	)		ER03-262-007
Columbus Southern Power Company)		
Indiana Michigan Power Company)		
Kentucky Power Company)		
Kingsport Power Company)		
Ohio Power Company, and)		
Wheeling Power Company)		
)		
Commonwealth Edison Company and)		
Commonwealth Edison Company of)		
Indiana, Inc.)		
The Dayton Power and Light Company)		
)		
American Electric Power Company, Inc. and	)	Docket Nos.	EC98-40-000
Central and South West Corporation	)		ER98-2770-000
	)		ER98-2786-000
)		
)		
Ameren Services Company	)	Docket Nos.	EL02-65-006
)		
Illinois Power Company	)	Docket Nos.	EL02-65-000 et al.
	)		RT01-88-016

FILED
OFFICE OF THE SECRETARY
03 SEP 23 PM 4:00
FEDERAL ENERGY
REGULATORY
COMMISSION

PREPARED DIRECT TESTIMONY
OF
COMMISSIONER LAURA CHAPPELLE
ON BEHALF OF
MICHIGAN PUBLIC SERVICE COMMISSION

SEPTEMBER 23, 2003

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**PREPARED DIRECT TESTIMONY
OF COMMISSIONER LAURA CHAPPELLE
ON BEHALF OF
THE MICHIGAN PUBLIC SERVICE COMMISSION**

Q. PLEASE STATE YOUR NAME, TITLE AND BUSINESS ADDRESS.

A. Laura Chappelle, Commissioner of the Michigan Public Service Commission.

My business address is 6545 Mercantile Way, Suite 14, Lansing, MI 48911.

1 Q. PLEASE DESCRIBE YOUR EXPERIENCE AND EDUCATIONAL
2 BACKGROUND.

3 A. I am currently serving as Commissioner of the Michigan Public Service
4 Commission for a term that runs through July 2, 2007. I served as Chairman of
5 the Michigan Public Service Commission ("MPSC") from January 16, 2001
6 through August 2, 2003. Prior to my appointment to the Commission, I served as
7 Deputy Legal Counsel for Governor John Engler. I have also served as
8 Regulatory Affairs Coordinator to the Michigan House Republicans, attorney for
9 former Michigan House Speaker, Paul Hillegonds, legislative aid for State
10 Senator, William Van Regenmorter, and as Assistant Prosecuting Attorney with
11 the Saginaw County Prosecutor's Office. I have also been an adjunct faculty
12 member at Lansing Community College and Michigan State University.

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14
15 I have a B.A. degree from the University of Michigan (1985) and J.D. from
16 Thomas Cooley Law School (1988).

17
18 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

19 A. The purpose of my testimony is to respond to the Commission's inquiry into the
20 impediments to utilities in joining the Midwest ISO or PJM and proposals for
21 resolving these impediments. The MPSC is fully committed to the development
22 of the RTO structure within the Midwest region. Regional coordination has
23 worked successfully in other areas of the country. We continue to support the
24 Commission in its efforts to expeditiously bring closure to a properly configured
25 RTO structure in the Midwest. The recent blackout underscores the strong
26 regional interdependence of the transmission grid throughout the Midwest and
27

1 how important regional cooperation and coordination are to both competitive and
2 reliable electric service.

3 Q. PLEASE EXPLAIN THE BACKGROUND OF THE MPSC'S INTEREST AND
4 INVOLVEMENT IN MIDWEST ENERGY MARKETS.

5 A. The MPSC has demonstrated a longstanding commitment to the establishment of
6 open access transmission service and competitive markets for sales of electric
7 energy. To achieve this vision, the MPSC has taken an active role, both as a
8 regulator in the State of Michigan and as an active party in proceedings before the
9 FERC.
10

11 Michigan's Customer Choice and Electricity Reliability Act (2000 PA 141; MCL
12 460.10 *et seq.*) was enacted by the Michigan Legislature and signed into law by
13 Governor John Engler in June of 2000. In the months that followed, the MPSC
14 issued the necessary orders to implement the new law. Full retail open access
15 began in Michigan on January 1, 2002.
16

17 The MPSC has consistently supported the Commission's efforts to increase access
18 to the transmission grid and the competitiveness of the electric generation market.
19 The MPSC filed comments supporting the issuance of Order No. 888.
20 Subsequent to Order No. 888, the MPSC actively promoted and participated in the
21 formation of an Independent System Operator ("ISO") to serve the Midwest. In
22 August of 1999, the MPSC joined with eight other state commissions to support
23 the timely development of Regional Transmission Organizations ("RTO").
24 Subsequent to the issuance of Order No. 2000, the MPSC was actively engaged in
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1 the collaborative process to determine whether RTOs of sufficient geographic
2 scope could be formulated to serve the Midwest and other parts of the country.

3
4 Two competing RTOs emerged from that process, the Midwest ISO and the
5 Alliance RTO. As the lead state commission on the Midwest ISO Advisory
6 Committee in 2001, the MPSC worked in tandem with our regional colleagues to
7 reach the MISO/Alliance Settlement Agreement that was approved by the
8 Commission on March 21, 2001. The Settlement permitted the formation of two
9 RTOs, and provided for an Inter-RTO Cooperative Agreement ("IRCA") that
10 would develop a seamless market in the region covered by the Alliance RTO and
11 the Midwest ISO.
12

13 Unfortunately, neither the Order No. 2000 collaborative process nor the
14 MISO/Alliance Settlement Agreement produced satisfactory results in the
15 Midwest. Instead of one large Midwest RTO (or two seamless RTOs), the
16 Alliance Companies and the Midwest ISO competed against each other in
17 forming separate transmission organizations. The end result was a patchwork of
18 service areas with RTO boundaries that made no geographic sense and created
19 barriers to the development of a competitive wholesale market for electricity
20 across the Midwest region.
21
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23 On November 30, 2001, the MPSC joined with fourteen other state agencies in
24 responding to the Commission's November 9, 2001 letter which contained several
25 questions related to RTO formation in the Midwest. The Midwest state
26 commissions filed joint comments with the Commission which outlined in detail
27

1 why multiple RTOs managed through seams agreements "has not worked and will
2 not work in the Midwest", as evidenced by the fact that little progress had been
3 made on implementing the IRCA. Moreover, the MPSC and the other
4 commissions outlined the problems caused by a lack of independence during the
5 start-up phase.
6

7 On December 20, 2001, the Commission rejected the Alliance RTO and required
8 the Alliance Transmission Owners to file a statement of their plans to join an
9 RTO.
10

11 Unfortunately, the resulting RTO choices by the former members of the Alliance
12 RTO bear no relationship to the geography of the Midwest or to economic logic.
13 Illinois Power, Commonwealth Edison and the AEP Operating Companies,
14 including Indiana Michigan Power Company that serves Michigan, all announced
15 their intention to join PJM rather than the Midwest ISO. The resulting
16 configuration has been described by one FERC Staff witness as resembling
17 "Swiss Cheese".
18

19 On July 31, 2002, the Commission issued its order conditionally approving the
20 RTO choices of the former Alliance Companies, subject to nine conditions,
21 including the following five that are of particular importance to the MPSC: (1)
22 that a single market across the two RTOs must be implemented by October 1,
23 2004; (2) that the North American Electric Reliability Council ("NERC") must
24 approve the Reliability Plans pursuant to which PJM and Midwest ISO will
25 coordinate their operations under the new configuration; (3) that a solution
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1 addressing the through and out rates between Midwest ISO and PJM must be
2 developed; (4) that certain of the former Alliance Companies seeking to join PJM,
3 along with PJM and Midwest ISO, provide a solution which will effectively hold
4 utilities in Wisconsin and Michigan harmless from any loop flows or congestion
5 that results from the proposed configuration; and (5) that PJM and Midwest ISO
6 must each file a statement agreeing to the conditions within 15 days of the July 31
7 Order, an implementation plan for achieving a common market by October 1,
8 2004, within 45 days, and frequent progress reports thereafter.³

10 The Commission explained that the former Alliance Companies' choices, standing
11 alone, appeared to produce unjust and unreasonable rates, terms and conditions
12 for transmission services, but that these conditions would ensure just and
13 reasonable rates, terms, and conditions for transmission services. The July 31
14 Order also notes that these conditions reflected areas which NERC concluded
15 needed to be addressed, as well as commitments made by the parties in order to
16 further the goal of reaching a region-wide common market as soon as possible.⁴

19 The Commission particularly found that one of the primary obstacles to RTO
20 formation has been rate pancaking for transactions crossing RTO borders. The
21 Commission stated that, in light of the former Alliance Companies' RTO choices,
22 the resolution of inter-RTO rates was fundamental to its decision to accept the
23 choices of Illinois Power, ComEd, and AEP to join PJM, and that resolving inter-
24

25 ³ See July 31 Order at P 35-37.

26 ⁴ *Id.* at P 35-36.
27

1 RTO rates was fundamental to establishing a single common market. Therefore,
2 the July 31 Order also instituted an investigation and hearing of inter-RTO rates
3 under Section 206 of the FPA before an administrative law judge in Docket No.
4 EL02-111, with regard to the rates for through-and-out service in the Midwest
5 ISO/PJM region and with respect to the protocols relating to the distribution of
6 revenues associated with such through-and-out service.⁵
7

8 On July 23, 2003, the Commission issued its Order on Initial Decision in Docket
9 No. EL02-111 finding that the proposed RTO choices and resulting configuration,
10 without conditions, would frustrate the realization of the goals of RTO formation
11 such as resolution of loop flow issues, effective management of congestion, and
12 enhanced reliability and efficiency.
13

14 In reaching its conclusion, the Commission found that by virtue of their location
15 and ties to their neighbors, the former Alliance Companies, through their failure
16 to join RTOs, and also through their proposed RTO choices, would create a
17 barrier that obstructs more efficient and competitive electricity markets and the
18 realization of adequate RTO scope and configuration in the region, thereby
19 denying the benefits of more efficient and competitive regional electricity markets
20 to customers in 21 states and one Canadian province. In addition, the
21 Commission expressly concluded that other evidence indicates that the entry of
22 the new PJM Companies and Illinois Power into PJM will result in Michigan and
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26 ⁵ *Id.* at P 49-50.
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1 Wisconsin being only partially contiguous with the rest of Midwest ISO. The end
2 result is that Michigan and Wisconsin would be required to pay pancaked rates in
3 order to wheel power through PJM from elsewhere in Midwest ISO.
4

5 Q. ARE THE CONDITIONS IMPOSED BY THE COMMISSION IN ITS JULY 31
6 ORDER SERVING AS IMPEDIMENTS TO FORMER ALLIANCE
7 COMPANIES JOINING AN RTO?

8 A. The former Alliance Companies that joined PJM, who now call themselves the
9 New PJM Companies, are likely to argue that some or all of the conditions
10 imposed by the Commission are an impediment to their joining an RTO. The
11 MPSC agrees with prior FERC rulings that these conditions are necessary and
12 should not be viewed as impediments.

13 Q. SHOULD ANY OF THESE CONDITIONS BE REMOVED?

14 A. No. The Commission has already held that RTO choices of the New PJM
15 Companies standing alone without conditions, appear to produce unjust and
16 unreasonable results. To illustrate this point, I have attached Exhibit No. MPSC-
17 2, a map of the resulting RTO configuration that assumes the Commission stays
18 with its conditional approval of the New PJM Companies' plan to join PJM. As
19 indicated, Michigan and Wisconsin are virtually isolated and cut-off from the
20 Southern part of the Midwest ISO. The resulting rate "seams" will interfere with
21 the natural boundaries of the market and the development of a common market.
22 Thus, the prompt elimination of through-and-out rates is essential to the
23 establishment of a common market by October 1, 2004. The condition to protect
24 entities in Michigan and Wisconsin from loop flow is critical to the MPSC. As
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1 recently confirmed by the Midwest ISO and PJM market monitors, the proposed
2 irregular geographic seam between PJM and the Midwest ISO will result in
3 significant electrical interactions, also known as loop flows, between the Midwest
4 ISO and PJM market areas. The Commission must ensure that Michigan is held
5 harmless from any adverse impacts upon system reliability, as well financial
6 impacts, caused by loop flow. Absent clear and detailed protocols, RTOs with
7 high degrees of electrical interaction are likely to dispatch generation without
8 regard to relevant constraints on each others' systems. The MPSC is very
9 concerned that under the *status quo*, with the former Alliance Companies
10 belonging to no RTO, the reliability of Michigan's transmission system can be
11 seriously compromised by loop flow. Moreover, if the New PJM Companies are
12 allowed to join PJM, rather than the Midwest ISO, loop flows will not be
13 internalized unless and until a joint and common Midwest ISO/PJM market is
14 fully functional. Also, along these lines the "hold harmless" provision is critical
15 to maintaining regional reliability in Michigan.

16 Furthermore, the recent blackout highlights the importance of NERC approval of
17 the Reliability Plans pursuant to which PJM and the Midwest ISO will coordinate
18 their operations under the new configuration.

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23 Q. IS THE POTENTIAL LOSS OF REVENUE RESULTING FROM THE
24 ELIMINATION OF THROUGH-AND-OUT RATES AN IMPEDIMENT TO
25 RTO DEVELOPMENT?

26 Judging by the amount of controversy and contentious litigation spawned by this
27 issue in Docket No. EL02-111, I would have to conclude that a Commission

1 resolution of this issue would remove a major impediment to the former Alliance
2 Companies joining an RTO. The Commission issued its order conditionally
3 approving the former Alliance Companies' RTO choices on July 31, 2002. The
4 parties have had more than a year to resolve and implement the conditions
5 imposed by the Commission. The New PJM Companies could not even agree on
6 the definition of "hold harmless" as it applied to Michigan and Wisconsin, let
7 alone implement such condition. While FERC has made progress by eliminating
8 through-and-out rates for the Midwest ISO and PJM in its recent order in Docket
9 No. EL02-111, efforts to totally eliminate through-and-out rates and to deal with
10 lost revenues remain unresolved. In my view, the fact that these issues remain
11 unresolved is a significant impediment to the former Alliance Companies joining
12 an RTO.
13
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15 Q. ARE YOU SUGGESTING THAT THE COMMISSION SHOULD REMOVE
16 THIS IMPEDIMENT BY APPROVING THE CLAIMS FOR LOST REVENUE?

17 A. No. The MPSC has been actively involved in the litigation of the lost revenue
18 issue. Based on the record in that proceeding it is clear that AEP, whose claim for
19 \$150 million represents the bulk of the claimed lost revenue, is considerably
20 inflated.
21

22 Q. WHY DO YOU CONCLUDE THAT AEP'S LOST REVENUE CLAIM IS
23 INFLATED?

24 A. There are several reasons for this conclusion. First, any lost revenue mechanism
25 that is based on a past period will over-recover from Michigan entities because
26 such a method fails to reflect the existence of new generation that has come on
27

1 line in Michigan, thereby causing a reduction to historical imports. Second, the
2 use of NERC Tag Data advocated by proponents of a lost revenue surcharge is not
3 an accurate method to calculate transmission revenues. This is demonstrated by
4 the fact that the estimates of lost revenue relied upon by the New PJM Companies
5 exceed at the actual transmission invoices paid by Michigan companies for
6 imports of power. For these reasons, I would urge the Commission *not* to give in
7 to the inflated claims for lost revenue. Due to these erroneous elements in the
8 calculation of lost revenues and the fact that responsibility for any such lost
9 revenues are falling disproportionately on Michigan and Wisconsin entities, it is
10 crucial for Michigan entities to be given the right to opt-out of any lost revenue
11 mechanism and instead pay the former through-and-out rates for actual imports
12 over a two-year transaction period.
13
14

15 Q. WHAT IS THE STATUS OF MICHIGAN UTILITIES' RTO MEMBERSHIP?

16 A. Michigan's two largest utilities, Consumers Power Company and Detroit Edison
17 Company, divested ownership of their transmission facilities. These facilities
18 were purchased by new owners and are operated as independent transmission
19 companies free from any affiliation with market participants. These two
20 companies, International Transmission Company and Trans-Elect, both belong to
21 the Midwest ISO. In addition, the Michigan utilities located in the Upper
22 Peninsula have joined Midwest ISO through the American Transmission
23 Company, an independent transmission company under the Midwest ISO.
24 Indiana Michigan Power Company is the only major investor-owned electric
25 utility in Michigan that has not joined an RTO.
26
27

1 Q. WHAT ABOUT THE ACTIONS BY THE VIRGINIA LEGISLATURE AND
2 THE KENTUCKY PUBLIC SERVICE COMMISSION PROHIBITING AEP
3 FROM TRANSFERRING FUNCTIONAL CONTROL OF THE
4 TRANSMISSION FACILITIES LOCATED IN THOSE TWO STATES TO
5 PJM?

6 A. With all due respect to my colleagues in other states, their decisions could have an
7 adverse impact upon the competitiveness and reliability of electric service in
8 Michigan, particularly if the actions of one or two states result in prohibiting all
9 AEP Operating Companies from joining an RTO. These issues need to be worked
10 out. In the meantime, I do not agree with AEP that the actions of two states can
11 prevent AEP's Operating Companies located in other states from moving forward
12 with joining an RTO. For example, Michigan's Legislature enacted a law
13 *requiring* AEP's affiliate serving Michigan, Indiana Michigan Power Company, to
14 divest itself of transmission lines or belong to an RTO. I see no reason why AEP
15 cannot comply with Michigan law. The MPSC has indicated its desire for AEP to
16 join an RTO on other occasions. On March 14, 2003 in ER03-262, the MPSC,
17 along with the Pennsylvania and Ohio state regulatory commissions, requested the
18 Commission to direct AEP to join an established RTO.

19
20 Q. AEP IS CLAIMING THAT ITS SYSTEM IS SO INTEGRATED THAT IT
21 CANNOT IMPLEMENT RTO MEMBERSHIP ON A STAND ALONE
22 OPERATING COMPANY BASIS. IS THIS AN ADEQUATE REASON FOR
23 EXCUSING AEP FROM RTO MEMBERSHIP?

24 A. I am not an expert in the integrated AEP system operations. However, I would
25 note that when Texas and Ohio implemented their retail open access program,
26 AEP requested in Docket No. EC01-130-000, authorization from the
27 Commission to separate AEP's Texas and Ohio generation assets from the

1 remainder of its integrated power pool so that generation in those two states could
2 be sold at market-based rates. I would like AEP to explain why it can separate its
3 system to accommodate market-based pricing for its generators but not to join an
4 RTO.
5

6 Q. COULD YOU PLEASE SUMMARIZE YOUR CONCLUSIONS.
7

8 A. All major transmission systems within the Midwest region must be fully
9 integrated into an RTO promptly. To accomplish this, the Commission should
10 continue to work expeditiously with the states to remove jurisdictional
11 impediments to RTO membership in a manner that effectively addresses RTO
12 configuration issues in the Midwest region. In the meantime, I would urge the
13 Commission to move forward with the elimination of all seams within the
14 Midwest region market area and the development of a common market applicable
15 to such market area. Once all seams are eliminated and a common market is in
16 place, consumers will benefit from a more competitive market for sales of
17 electricity.
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19
20 Q. DOES THIS CONCLUDE YOUR TESTIMONY?
21

22 A. Yes.
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STATE OF MICHIGAN)
) SS.
COUNTY OF _____)

BEFORE ME, the undersigned authority, on this day personally appeared LAURA
CHAPPELLE, who being by me first duly sworn, on oath and deposes and says:

That she is the LAURA CHAPPELLE, offering the foregoing Direct Testimony of Laura
Chappelle and that all statements of fact contained therein are true and correct to the best of her
knowledge, information and belief.


Laura Chappelle

Subscribed and sworn to before me this 23rd day of September, 2003.


Tina L. Bibbs, Notary Public
Ingham County, Michigan
My Commission Expires: 11/13/2003

Midwest ISO Footprint

- ☐ - Midwest ISO members
as of 9/15/03, plus
the GridAmerica
Companies
- ☐ - Other Former Alliance
Companies

